No. 15-233

IN THE

Supreme Court of the United States

THE COMMONWEALTH OF PUERTO RICO, ALEJANDRO GARCÍA PADILLA, as Governor of the Commonwealth of Puerto Rico, and CÉSAR MIRANDA RODRÍGUEZ, as Secretary of Justice of the Commonwealth of Puerto Rico,

Petitioners,

v.

FRANKLIN CALIFORNIA TAX-FREE TRUST, et al.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the First Circuit

BRIEF OF FUNDACIÓN ÁNGEL RAMOS, INC.; FUNDACIÓN COMUNITARIA DE PUERTO RICO, INC.; MIRANDA FOUNDATION; TITÍN FOUNDATION, INC.; INICIATIVA COMUNITARIA DE INVESTIGACIÓN, INC.; PUERTO RICO DOWN SYNDROME FOUNDATION, INC.; CORPORACIÓN DE LA FONDITA DE JESÚS; ASESORES FINANCIEROS COMUNITARIOS, INC.; CREARTE, INC.; ALIANZA LAURA APONTE POR LA PAZ SOCIAL (ALAPAS), INC.; FUNDACIÓN CHANA GOLDSTEIN Y SAMUEL LEVIS, INC.; POLITÉCNICO AMIGÓ, INC.; INSTITUTO ESPECIAL PARA EL DESARROLLO INTEGRAL DEL INDIVIDUO, LA FAMILIA Y LA COMUNIDAD, INC.; AND PROYECTO NACER, INC., AS *AMICI CURIAE*, IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether Chapter 9 of the federal Bankruptcy Code, which does not apply to Puerto Rico, nonetheless preempts a Puerto Rico statute creating a mechanism for the Commonwealth's public utilities to restructure their debts.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	vi
INTEREST OF THE *AMICI CURIAE*	1
STATEMENT OF THE CASE	2
SUMMARY OF ARGUMENT	2
ARGUMENT	3
I. WITHOUT A MECHANISM TO RESTRUCTURE THE DEBT OF ITS PUBLIC CORPORATIONS LIKE THE ONE CREATED BY THE RECOVERY ACT, THE GOVERNMENT OF PUERTO RICO WILL BE FORCED TO REDUCE EVEN FURTHER ITS FINANCIAL SUPPORT TO THIRD SECTOR ORGANIZATIONS THAT PROVIDE DIRECT ESSENTIAL SERVICES TO THE PEOPLE OF PUERTO RICO	3
A. The General State of Puerto Rico's Economy	4
B. The Burden of Public Corporations to the Local Economy	5
C. Puerto Rico's Economic and Fiscal Outlook Continues to Worsen	7
D. An Overview of the Third Sector in Puerto Rico	9
E. The Third Sector Plays a Crucial Role in Providing Basic Services to the People of Puerto Rico	11

TABLE OF CONTENTS—Continued

	Page
F. The Impact of NPOs in Education	12
G. Services that NPOs Provide to the Elderly	13
H. The Role of the Third Sector in the Economy of Puerto Rico	13
I. Impact of the Economic and Fiscal Crisis on NPOs	15
J. NPOs Need the Continued Financial Support of the Government of Puerto Rico	18
II. PUERTO RICO'S INABILITY TO RESTRUCTURE THE DEBT OF ITS PUBLIC CORPORATIONS CURTAILS ITS ABILITY TO GUARANTEE THE HUMAN RIGHTS OF ITS CITIZENS	19
A. Fair Debt Restructuring is Essential for the Protection of Human Rights	19
B. Although Puerto Rico is not a State of The United States, it Should be Treated as a State Under a Fair Constitutional Interpretation of the Due Process and Equal Protection Clauses, of The Fifth And Fourteenth Amendments	21
III. THE RECOVERY ACT IS NOT PREEMPTED BY CHAPTER 9 OF THE FEDERAL BANKRUPTCH CODE	23

TABLE OF CONTENTS—Continued

Page

A. The Preemption Analysis of the Opinion Below is Erroneous and Usurps the Right of the Commonwealth of Puerto Rico to Exercise its Police Power to Protect its Citizens 23

B. The Opinion Below Concedes that the Legislative History of the 1984 Amendments to the Bankruptcy Code is Silent as to the Reasons for the Exclusion of Puerto Rico from Chapter 9 25

C. The Opinion Below Failed to Consider the Most On-Point Precedent on the Correct Application of Preemption Analysis 26

CONCLUSION 27

TABLE OF AUTHORITIES

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Alessi v. Raybestos-Manhattan, Inc., 451 U.S. 504 (1981)	25
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11 U.S.C. Ch. 9 ..... 3, 24, 25

11 U.S.C. § 903(1) 3

TABLE OF AUTHORITIES—Continued

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INTEREST OF THE *AMICI CURIAE*[1]

The *amici curiae* in this case are a group of entities comprised by four Puerto Rico private foundations[2] that fund, among others, the operations of ten non-profit organizations[3] that provide services directly to the people and communities in Puerto Rico.

As a result of Puerto Rico's inability to restructure the debts of its public corporations resulting from the decision below, the *amici* and other foundations and non-profit organizations in Puerto Rico will be directly affected because the government of Puerto Rico will be forced to reduce the financial support that it provides to these entities.

Without the continued support from the government, the *amici* and other foundations and non-profit organizations will not be able to provide essential services

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[1] Pursuant to Supreme Court Rule 37.3(a), the *amici curiae* state that they have received written consent from all parties to file this brief. The *amici curiae* further state that, no counsel for any party authored this brief in whole or in part; and that no person or entity, other than *amici* and their counsel, made a monetary contribution intended to fund the preparation and submission of this brief.

[2] These foundations are: Fundación Ángel Ramos, Inc.; Fundación Comunitaria de Puerto Rico, Inc.; Miranda Foundation and Titín Foundation, Inc.

[3] These non-profit organizations are: Iniciativa Comunitaria de Investigación, Inc.; Puerto Rico Down Syndrome Foundation, Inc.; Corporación de la Fondita de Jesús; Asesores Financieros Comunitarios, Inc.; Crearte, Inc.; Alianza Laura Aponte por la Paz Social (ALAPAS), Inc.; Fundación Chana Goldstein y Samuel Levis, Inc.; Politécnico Amigó, Inc.; Instituto Especial para el Desarrollo Integral del Individuo, la Familia y la Comunidad, Inc.; and Proyecto Nacer, Inc.

to some of the poorest and most vulnerable people in Puerto Rico.

STATEMENT OF THE CASE

This case involves the Commonwealth of Puerto Rico's attempt to exercise the most basic form of traditional state police power. Puerto Rico enacted the Recovery Act in response to the reality that the public corporations used by the Commonwealth to provide essential services like electricity and water cannot pay their debts and are cornered by their creditors. The people of Puerto Rico literally cannot survive without receiving these services, and the Commonwealth has the obligation to exercise its police power to respond to this crisis.

In addition, this case has important ramifications on the interpretation of preemption principles that lie at the very core of Federalism. In concluding that the Recovery Act was preempted by § 903(1) of the Bankruptcy Code, the opinion below disregarded the analytical framework set forth by this Court for the determination of the existence of preemption in a way that is catastrophic for Puerto Rico.

SUMMARY OF ARGUMENT

The non-profit sector provides direct services that are essential for the survival and well being of some of the poorest and most vulnerable people in Puerto Rico. This sector depends on the government. To the extent that the Commonwealth of Puerto Rico is not allowed to restructure the debt of its public corporations, it will be forced to continue cutting the funding of these organizations, which in turn, will not be able to provide essential services to the people.

Puerto Rico needs a legal framework like the one created by the Recovery Act in order to restructure the debt of its public corporations. To the extent that Congress expressly decided to leave Puerto Rico out of the coverage of Chapter 9 of the Bankruptcy Code, there is no basis to conclude that the Recovery Act is preempted.

ARGUMENT

I. WITHOUT A MECHANISM TO RESTRUCTURE THE DEBTS OF ITS PUBLIC CORPORATIONS LIKE THE ONE CREATED BY THE RECOVERY ACT, THE GOVERNMENT OF PUERTO RICO WILL BE FORCED TO REDUCE EVEN FURTHER ITS FINANCIAL SUPPORT TO THIRD SECTOR ORGANIZATIONS THAT PROVIDE DIRECT ESSENTIAL SERVICES TO THE PEOPLE OF PUERTO RICO

Puerto Rico's inability to restructure the debt of its public corporations as a result of the decision below has a profound impact at all levels of Puerto Rican society. Puerto Rico's "Third Sector", comprised mainly of non–profit organizations ("NPOs") that provide services and social development structure to the Island's most vulnerable individuals and communities is particularly harmed by this decision. Its continued existence is now threatened by the effects of this decision on the Island's economy.

A. The General State of Puerto Rico's Economy

Puerto Rico has experienced a prolonged economic contraction since the year 2000. Just between 2006 and 2013, it has faced an average annual contraction of 1.7%. It is estimated that 200,000 jobs[4] have been lost, and that 46.2% of the Island's population lives below the federal poverty line.[5] The unemployment rate in Puerto Rico for 2014 was 14.4%.[6] Puerto Rico's annual mean wage is $27,510, well below that of Mississippi, the poorest state in the United States.[7]

This precarious economic situation has been exacerbated by the largest migration of Puerto Ricans in more than fifty years. Puerto Rico's population has shrunk by more than 82,000 between 2000 and 2010, approximately 2.2% of the general population. From 2010 to 2014, it is estimated than an additional 150,000 Puerto Ricans have left the Island. Close to 60% of these

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[4] Puerto Rico's Planning Board Economic Report to the Governor of Puerto Rico of 2013 presented December 24, 2014.

[5] *See U.S. Census Bureau, American Community Survey 1-Year Estimates (2014) http://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ACS_14_1YR_S1903&prodType=table.*

[6] *Departamento del Trabajo y Recursos Humanos, Tablas Estadísticas, available at* http://www.mercadolaboral.pr.gov/Tablas_Estadisticas/Fuerza_Trabajadora/T_Serie_Historica.aspx

[7] Mississippi's annual mean wage is $36,750, Bureau of Labor Statistics of the US Labor Department (updated on March 25, 2015). (NOTE: The American Community Survey reported that the median household income in Puerto Rico was $18,928 as of 2014. However, the US Census Bureau itself admitted that there is a tendency for people to underreport household income. The *amici* decided to emphasize the latter in order to provide a more accurate picture of the current situation in Puerto Rico.

migrants are between the ages of 18-54, and 29% between the ages of 0 and 17 years. This means that Puerto Rico is losing both its current and future workforce. By the year 2020, it is estimated that a substantial part of the Island's population will be 65 or older[8].

The government of Puerto Rico also faces immense fiscal challenges. According to a 2014 New York Federal Reserve economic study, Puerto Rico's total public debt is approximately $72 billion. The debt of its public corporations accounts for 36.4% of the total general government debt.

B. The Burden of Public Corporations to the Local Economy

Puerto Rico's Electric Power Authority ("PREPA") is, for all practical purposes, the sole electric power provider in the Island. The cost of electricity in Puerto Rico in kilowatt/hours is the second most expensive in the United States.[9] Its infrastructure is both outdated and inefficient. PREPA's inability to invest in more efficient, cost effective and diversified infrastructure has rendered it extremely dependent on imported oil, as confirmed by economic reports from the New York Federal Reserve and Anne Krueger, former Director of the International Monetary Fund[10].

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[8] Estimates based on the 1990, 2000 and 2010 Censuses carried out by P.R's Planning Board in conjunction with US Census Bureau.

[9] According to the U.S. Energy Information Administration (http://www.eia.gov/electricity/state/).

[10] See "*An update on the Competitiveness of Puerto Rico's Economy*", NY Fed. Reserve Bank, July 31, 2014 and Krueguer, Teja, and Wolfe, "*Puerto Rico, A Way Forward*", published June 29, 2015.

PREPA's debt constitutes an impediment for making crucial investments in Puerto Rico's infrastructure. According to its last audited report, PREPA only has $16 million for capital improvements[11]. In addition, PREPA has also experienced consecutive operational deficits ranging from $272 and $346 million between 2011 and 2013.

Other public corporations, namely the Puerto Rico's Transport Authority ("PRTA") and the Aqueduct and Sewers Authority ("PRASA"), place a similar burden on the Island's economy. Both operate as publicly sanctioned state monopolies, have deficient and costly infrastructure, and force a heavy burden on taxpayers. Their respective fiscal situations are already impacting the economy. For example, Puerto Rico's Legislature has been forced to significantly raise taxes on petroleum-based products *twice* during the past year in an attempt to save PRTA's finances[12]. To make matters worse, Puerto Rico's population is extremely dependent on automobiles and PRTA has been unable to develop a comprehensive and reliable public transportation system. While these shortcomings have been signaled out as yet another reason for Puerto Rico's economic hardships,[13] elected officials have been forced to resort to extremely unpopular and costly impositions

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[11] "*Financial Statements, Required Supplementary information and Supplemental Schedules. Puerto Rico Electric Power Authority*", Ernst and Young LLP, January 16, 2014.

[12] See Public Law #1 of 2015. Also, see following news article that sufficiently illustrate how difficult it was to pass this law due to intense popular opposition: http://www.primerahora.com/noticias/gobiernopolitica/nota/arduoelcaminoparalaaprobacionde lacrudita-1051827/

[13] "An Update on the Competitiveness of Puerto Rico's Economy", Federal Reserve Bank of New York, July 31, 2014.

just to keep PRTA's head above water. Similarly, significant rate increases on water bills have also been implemented in order to protect PRASA.

C. Puerto Rico's Economic and Fiscal Outlook Continues to Worsen

Since the presentation of our *amici* brief at the petition stage on September 23, 2015, the fiscal outlook for the government of Puerto Rico has deteriorated even further. The Puerto Rico Financing Infrastructure Authority (PRIFA) has joined the Puerto Rico Public Finance Authority (PFC) in defaulting on debt service payments[14]. By January 2016, the two entities had failed to meet a total of $ 100.8 million in debt payments: $ 64.9 million from PFC (which first defaulted in August 2015 and has failed to make monthly debt service payments since then) and $ 35.9 from PRIFA (which first defaulted on January 2016).

In November 2015, the Governor of Puerto Rico ordered the Treasury Department to implement a constitutional "clawback" provisions for $164 million in revenues that supported debt obligations of PRIFA, the Highway and Transportation Authority (HTA) and the Convention Center District Authority (CCDA) in order to honor the Commonwealth's Constitutional obligations[15]. As a result, Assured Guaranty and Ambac Financial, insurers of Puerto Rico-issued debt, have sued the Government of Puerto Rico in the

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[14] Giel, D., "*Puerto Rico will default on portion of $1B in bonds on Monday: Officials*", CNBC, December, 31, 2015, http://www.cnbc.com/2015/12/30/puerto-rico-will-default-on-small-portion-of-the-1b-in-bonds-due-monday-officials.html

[15] Administrative Bulletin Num. OE-2015-046.

United States District Court for the District of Puerto Rico, in what could be the first in a series of creditor lawsuits that will move forward in the absence of a statutory framework allowing for the restructuring of this debt[16]. HTA and CCDA are expected to fail to meet their debt service payments in the coming months.

The Commonwealth paid the debt service on its General Obligation debt (GO's) in January 2016, after taking extraordinary emergency liquidity measures which, besides the "clawback", included: borrowing $ 400 million in emergency loans from its own state insurance companies and workers compensation funds; halting $93 million of monthly GO's set asides; deferring payment of tax refunds for the 2014 tax year; and postponing payments to service suppliers, including nonprofits. As of December 31, 2015, it is estimated that the accounts payable of the government have increased to $ 1.8 billion[17].

In the meantime, the Puerto Rico Treasury Department has revised downward its revenue estimates for fiscal year 2016 from $ 9.46 billion to $ 9.21 billion. The decrease in projected revenues, as well as an expected one-year delay in the assumed start of economic growth, has lead the GDB to increase its estimated 5-year financing gap to $ 27.9 billion, an

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[16] *"Comienzan demandas por el "clawback" y el impago"*, Noticel, Jan, 8 2016 http://www.noticel.com/noticia/185251/comienzan-las-demandas-por-el-clawback-y-el-impago-documento.html

[17] Working Group for the Fiscal and Economic Recovery of Puerto Rico, *"Puerto Rico Fiscal and Economic Growth Plan: Update Presentation"* January 18, 2016

increase of $ 2.1 billion since the release of the original Fiscal and Economic Growth Plan[18].

D. An Overview of the Third Sector in Puerto Rico

Puerto Rico's Third Sector directly provides services that are essential for the survival and well-being of some of the poorest and most vulnerable people in Puerto Rico. Without the Third Sector, most of these individuals and their communities would lack access to essential services. In addition, this sector provides mechanisms for civic participation to ensure appropriate public policies, government accountability and transparency, and provide independent analysis to inform the public debate.

Within the Third Sector, NPOs are involved in a wide range of activities and interests, including health promotion, education, arts and culture, social assistance, economic development, environmental protection, human rights, policy analysis, and civic engagement. Third Sector organizations include foundations, community-based organizations, museums, cooperatives, policy think tanks, and research enterprises. They have emerged as a result of the initiative of several concerned individuals who desired to improve the quality of life in Puerto Rico. Unlike the private sector, whose concern is the generation of profits, and the governmental sector, which protects the general welfare of all residents, the Third Sector harnesses

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[18] Working Group for the Fiscal and Economic Recovery of Puerto Rico, "*Puerto Rico Fiscal and Economic Growth Plan:*" September 9, 2015

and creates private social capital to improve the quality of life of the less fortunate.

The Third Sector serves as advocates and provides services to a wide variety of groups representing the most vulnerable portions of the Island's population. These groups include: high-risk and abused children, the homeless, persons living with HIV, drug addicts and alcoholics, single mothers, pregnant teenagers, victims of domestic violence, children with special needs, and the elderly[19]. NPOs integrate the community into their decision-making processes, and involve volunteer support to increase the talent pool and decrease the cost of the services they provide.

This NPO model of promoting both community involvement and volunteer support has been extremely successful and beneficial for Puerto Rico because it creates a more participative and committed community. NPOs also collect valuable demographic information, and examine the impact of their programs to encourage the adoption of these innovative practices in other communities within the Island.

As a society that needs more socially centered and empathic legislation, Puerto Rico cannot afford to lose these essential and participatory mechanisms as a part of the development of its public policies. NPOs provide essential information to legislators and other policy makers in Puerto Rico, collected on the basis of their day-to-day work with the groups they serve. Each of the NPOs that comprise the group of *amici* in

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[19] Study of the Non Profit Sector in Puerto Rico, prepared by the company Estudios Técnicos Inc. in 2015 (hereafter the *2015 Non Profit Sector Study*), *available at* http://www.estudiostecnicos.com/projects/orgssinlucro/pdf/Informe%20final%20OSFL%202015.pdf

this case, represents and caters to the specific needs of the particular group and communities each serve, which is something that no governmental agency in Puerto Rico is able to do directly.

Puerto Rico's acute economic crisis has underscored the importance of the Third Sector. The amount of resources spent by NPOs in providing assistance to the underprivileged in Puerto Rico has almost doubled in the past eight years. In 2007, there were around 6,300 NPOs in Puerto Rico. Today, there are more than 11,570 such organizations impacting the lives of one in every five residents in Puerto Rico (which is close to 700,000 residents of Puerto Rico). This sector is also responsible for 6.6% of the National Gross Income, and generates over 150,400 jobs[20]. The Third Sector represents 16% of the employed citizenry, which is a larger share of the employment than that of the financial, construction and manufacturing sectors.

E. The Third Sector Plays a Crucial Role in Providing Basic Services to the People of Puerto Rico

The Third Sector in Puerto Rico is a varied community that provides a broad range of assistance to disadvantaged individuals and communities that benefit greatly from services that would not be otherwise accessible to them and which satisfy specific needs that would otherwise go unattended.

With an increasing number of individuals and families living below the poverty line, these services become even more significant and crucial to Puerto Rico. NPOs are having the greatest impact in the areas of education, health, housing, environment, and social services. Some

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[20] *2015 Non Profit Sector Study 92.*

NPOs are directly contracted by public agencies, while others provide their services without intervention from the government. The principal agencies of the government of Puerto Rico that maintain contracts with NPOs are the Family Department and the Department of Education. Collaboration between the government and the Third Sector is highly beneficial for Puerto Rico and its economy. In light of the current economic crisis in Puerto Rico and the resulting fiscal austerity policies adopted by its government, these alliances between the public and the Third Sector are essential to the reduction of governmental costs.

F. The Impact of NPOs in Education

A study by "Kids Count Data Book" and the Institute for the Development of the Youth in Puerto Rico showed that 38% of adolescents in Puerto Rico fail to timely graduate from high school, and that 44% of its children fail to attend preschool.[21] Some of the more effective NPOs in Puerto Rico provide remedial services for this population and help school dropouts to finish high school. The *2015 Non Profit Sector Study* concluded that 44.8% of NPOs in Puerto Rico are providing educational services. Out of the total number of NPOs that provide educational services, 68.8% do so directly to students that are at risk of abandoning school or have already done so. Some of these programs include counseling, vocational courses and alternative education. The impact these organizations are having on this section of the Island's

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[21] *2015 KIDS COUNT Data Book 43 (2015) available at:* http://www.aecf.org/m/resourcedoc/aecf-2015kidscountdatabook-2015.pdf

population is significant, and governmental support is essential to secure their continued existence.

G. Services that NPOs Provide to the Elderly

According to the *2015 Non Profit Sector Study*, the elderly is one of the groups that benefits the most from the services provided by the Third Sector.[22] The United States Census Bureau (USCB) estimates that 17.4% of the total population in Puerto Rico is 65 years or older. 39.7% of this population lives below the poverty line along with an estimated 489,000 children under the age of 18, which accounts for 57% of the population in that age range.[23] The Island's stagnant economy has motivated many young families to leave. As a result, the elderly population has been growing and is expected to grow further as job creation, salaries and benefit levels decline.

H. The Role of the Third Sector in the Economy of Puerto Rico

According to the *2015 Non Profit Sector Study*, the Third Sector employs an estimated 150,410 people in Puerto Rico. This accounts for 16% of the total employment in Puerto Rico. This study also estimates the sector's employees' total salary at $2,194 million[24], which is the equivalent to for 3.1% of Puerto Rico's Gross National Product (GNP). This estimate increases to a 6.6% of the GNP when one adds the value of the

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[22] *2015 Non Profit Sector Study 88, 90.*

[23] *See U.S. Census Bureau, 2009-2013 5-Year American Community Survey available at* http://factfinder.census.gov/faces/nav/jsf/pages/index.xhtml

[24] NPOs contribute $258,126,640 and $964,126,800 in the areas of education and health, respectively. *2015 Non Profit Sector Study 121.*

sector's impact and the voluntary service provided[25]. Voluntary service is an essential characteristic of NPOs because it enables a reduction of costs in the services they provide. The Third Sector benefits from around 400,000 volunteers. The estimate value of voluntary service in the non-for-profit sector in Puerto Rico is $356 million.[26] As a result, NPOs are able to provide services comparable to those provided by the government since they maximize every dollar they raise.

Many of the services provided by NPOs would be too expensive for the government to provide. On the other hand, the consequences of failing to provide such services would surely be too damaging and difficult to quantify. Through the work of NPOs, the government is able to reduce expenses and make services more accessible to the people who need them. Furthermore, the *2015 Non Profit Sector Study* concluded that the government saves around $6.00 for every dollar it gives to NPOs for health services, and $19.00 for every dollar given to provide educational services. This shows that NPOs' services are more cost-effective, not only because they are more efficient than the government, but also because they benefit from an operational structure that is different and more flexible than that of the government.[27]

Although the Third Sector is an important strategic partner to the government since it provides services that the government simply cannot, this support could disappear if Puerto Rico has no choice but to make drastic budget cuts in order to service the debt. By supporting and investing in the Third Sector, the

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[25] *2015 Non Profit Sector Study 115,121-122.*

[26] *2015 Non Profit Sector Study 121.*

[27] *2015 Non Profit Sector Study 126-127.*

government saves money and secures services for one in every five individuals in Puerto Rico.

I. Impact of the Economic and Fiscal Crisis on NPOs

NPOs have already been severely affected by the economic and fiscal crisis. Private donations have dried up and the fundraising capability of these entities has diminished as a result of the economic downturn. NPOs have been forced to invest time and effort defending their public funding before a government that is desperately trying to raise the resources necessary to meet the demands of its creditors. It is therefore unquestionable that the fiscal state of Puerto Rico's public corporations has and will continue to have, a direct impact on the economy of the Island and on its overall fiscal health.

According to the *2015 Non Profit Sector Study*, the fiscal condition of most NPOs is as dire as that of the local economy. From 2006 to 2014, NPOs have reported an annual contraction of 17.5%[28]. These numbers show a direct correlation between the economic crisis and the financial health of these NPOs. This is not surprising since the majority of NPOs depend on private donations, fundraisers and self-sustaining activities.

Admirably, Puerto Rico's Legislature preserved some public funding for NPOs in the 2015-16 budget, after the NPOs mobilized to protest the cuts included

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[28] Based on an interview of 400 NPOs. Though there are more than 11,500 NPOs in Puerto Rico, the ones that were interviewed in this study are among the larger ones on the Island. Although the study could not reach a larger number of NPOs, the fact is that even the larger ones are experiencing such dramatic contractions, thus, one can safely assume that smaller, unknown NPOs are experiencing similar or greater hardships.

in the original budget proposal[29]. During that process, many NPOs emphasized that without this public funding, which is charged to the Island's General Fund,[30] they would not be able to survive the current economic climate.

The austerity measures taken by the government of Puerto Rico have already started to affect the non-for profit sector. Due to reduced revenue projection, as recently as January 13, 2016, the government's Office of Management and Budget (OMB) issued a determination reducing the amount of "special legislative grants" to various governmental entities and important nonprofit institutions. The total reduction was $254 million.[31]

The effect of this reduction has already affected the services provided by these organizations, and some have come so far as to indicate that they will completely shut down their operations. An example of an organization contemplating such drastic action is the Boys and Girls Club of Puerto Rico (BGCPR). This organization offers after-school programs to children and teenagers in disadvantaged communities.[32]

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[29] http://www.elnuevodia.com/noticias/locales/nota/organizacionessinfinesdelucroprotestaranenelcapitolio-2052557/(Translated title of news article: "NPOs will protest tomorrow in front of the Capitol").

[30] See Joint Resolution for of the General Budget for the 2015-16 Fiscal Year (RCC 747).

[31] Cortés Rico, R. "*OGP ajusta el gasto público*", El Nuevo Día, January 14, 2016 (printed version), pp. 4-5.

[32] Del Valle Hernández, S., "*Recorte de fondos dejaría sin servicios a cientos de menores del Boys and Girls Club*", Primera Hora, Octubre 16, 2015, http://www.primerahora.com/noticias/

In October 2015, the president of this organization announced that three clubs within the San Juan area had to close their doors due to lack of funds. An agreement with the Administration for Public Housing allowed them to extend their operations for an additional 60 days. On December 12, 2015, the Municipality of San Juan formalized an alliance with the BGCPR whereby the Municipality of San Juan allocated certain donations to these clubs in order maintain their operation.

Unfortunately, even such an important contribution is not sufficient to guarantee the continued existence of the BGCPR, and the situation is even more precarious for other the non-profit organizations that have not been able to secure similar assistance. If these three clubs effectively close, over 800 children and teenagers in the capital city of San Juan would be affected. More than 700 nonprofit organizations in Puerto Rico are facing similar or even more serious difficulties.

Other non-profit organizations affected by the $254 million reduction in the of special legislative grants include: Iniciativa Comunitaria de Investigación (serving population with drug related problems and the homeless); the Fondita de Jesús (helping the homeless in the reintegration to their communities and providing basic necessities); the Island's three main museums (Puerto Rico Museum of Art, Ponce Art Museum and the Contemporary Museum); Instituto Nueva Escuela (promoting academic excellence and social change in disadvantage communities); and Programa Alianza para Educación Alternativa

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(focusing on alternative education through different NGOs, including Centro Sor Isolina Ferré, ASPIRA, PECES, Nuestra Escuela).[33]

J. NPOs Need the Continued Financial Support of the Government of Puerto Rico

In order to operate and provide services, NPOs are highly dependent on donations from individuals, private corporations and the government of Puerto Rico. Within the Third Sector, private foundations that do not provide direct services to the public are also an essential source of funds for NPOs. These foundations provide donations and grants to help NPOs with operational and program expenses. But while the economic support that these foundations give to NPOs is essential, it cannot replace that of the government.

According to the *2015 Non Profit Sector Study*, approximately 38.0% of NPOs receive funds from municipalities, the Legislative Assembly or the central government.[34] This makes the government of Puerto Rico the third most frequent source of funding for NPOs, following individual donors and fundraising activities.

Puerto Rico's economic decline has greatly affected the Third Sector. The fiscal austerity programs adopted by the government of Puerto Rico to face the crisis have produced significant cuts in the funds appropriated for NPOs in the 2015-2016 budget.

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[33] Cortés Rico, R. "*OGP ajusta el gasto público*", El Nuevo Día, January 14, 2016 (printed version), pp. 4-5.

[34] *2015 Non Profit Sector Study* 92.

In light of the foregoing, it is undeniable that the survival of the Third Sector is tied to Puerto Rico's ability to restructure the debt of its public corporations.

II. PUERTO RICO'S INABILITY TO RESTRUCTURE THE DEBT OF ITS PUBLIC CORPORATIONS CURTAILS ITS ABILITY TO GUARANTEE THE HUMAN RIGHTS OF ITS CITIZENS

A. Fair Debt Restructuring is Essential for the Protection of Human Rights

There has been ample recognition that the lack of timely and fair debt restructuring processes can have a negative impact that goes far beyond the financial realm. Many times, over-burdened States are locked in downward spirals that prevent them from investing in their economy as a result of their debt obligations, notwithstanding the fact that they need to improve their economy in order to make their debt sustainable.

There has been an ever-growing international consensus that such downward spirals have endangered the human rights in those countries. The lack of access to a sensible and fair debt restructuring mechanisms results in the inability of the government to provide basic services such as water, electricity, or food distribution.

These concerns have been reflected in various in-depth studies submitted to the United Nation's Human Rights Council since the year 2010.[35] These studies

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[35] See "Report of the independent expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights" United Nations, GAOR, 14th Session, A/HRC/14/21. Also, "Report of the Independent Expert on the effects of foreign debt and other related international

have shown that countries that cannot properly restructure their substantial debts have difficulties guaranteeing the human rights of its citizens. On the other hand, countries that have been able to restructure their debt have experienced significant socioeconomic benefits such as increased school enrollments due to abolition of school access fees, and the provision of healthcare subsidies.

Even the World Bank and the International Monetary Funds have recognized the positive impact of debt relief in "[. . .] creating the fiscal space necessary for poverty- reducing expenditure and economic developments [. . .]".[36] Hence, there has been a positive correlation between debt relief, economic growth and promotion of human rights.

The United Nations recently adopted a resolution by an overwhelming majority that established certain basic principles that should guide all sovereign debt restructuring processes.[37] These guiding principles include concepts like sustainability and fairness in order to assure that States can guarantee human rights of its citizens while also protecting creditor's rights.

The public corporations in Puerto Rico need a legal framework that allows them to restructure their debt precisely because they are responsible for providing

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financial obligations of States on the full enjoyment of all human rights [. . .]" United Nations, GAOR, 20TH Session, A/HRC/20/23.

[36] "Report of the independent expert on the effects of foreign debt and other related international financial obligations [. . .]" United Nations, GAOR, 14th Session, A/HRC/14/21, p.11.

[37] "Basic Principles on Sovereign Debt Restructuring Processes", United Nations, GAOR, 69th Session, A/69/l.84. Voting was 136 in favor, 6 against and 41 abstentions.

vital utilities such as water and electricity to the people of Puerto Rico. In fact, Puerto Rico's inability to restructure the debt of its public corporations, particularly the debt of PREPA, could force a significant portion of the Island's population to live without adequate access to electric energy. Such deprivation would certainly amount to a violation of the dignity and the human rights of these Puerto Ricans, according to the European Convention on Human Rights.[38]

Furthermore, the Third Sector also aids the government of Puerto Rico in guaranteeing basic, internationally recognized human rights. Article 25 of the United Nations Universal Declaration of Human Rights recognizes that "[e]veryone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age . . ."[39] In Puerto Rico, more than half of the services provided by the Third Sector fall within this category.

B. Although Puerto Rico is not a State of The United States, it Should be Treated as a State Under a Fair Constitutional Interpretation of the Due Process and Equal Protection Clauses, of The Fifth And Fourteenth Amendments

The exclusion of Puerto Rico from the protection of the bankruptcy laws or from a comparable legal remedy

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[38] *See* Luis A. Avilés, *Electric Energy Access In European Union Law: A Human Right?*, 19 Colum. J. Eur. L. F. (2012).

[39] The Universal Declaration of Human Rights, http://www.un.org/en/documents/udhr/

via a rigid and inequitable judicial interpretation of the term "state" could be considered a violation of the principle of equal protection under the Fifth and Fourteenth Amendments.

Note that in *Bolling v. Sharpe*, 347 U.S. 497 (1954), a companion case to *Brown v. Board of Education*, 347 U.S. 483 (1954), the schools of the District of Columbia were desegregated even though Washington D.C. is not a "state". In that case, the court unanimously decided that while the Equal Protection Clause of the Fourteenth Amendment, cited in *Brown* to declare segregation unconstitutional, did not apply in the District of Columbia because it was not a "state", the Fifth Amendment did apply.

The Court concluded that "the concepts of equal protection and due process, both stemming from our American ideal of fairness, are not mutually exclusive." *Bolling v. Sharpe*, 347 U.S. 499. While equal protection is a more explicit safeguard against discrimination, the Court stated that "discrimination may be so unjustifiable as to be violative of due process." *Id.* Referring to the technicalities raised by the case's location in the District of Columbia, the Court held that, in light of their decision in *Brown*, it would be "unthinkable that the same Constitution would impose a lesser duty on the Federal Government." *Id.*

Indeed, Puerto Rico is considered a state for purposes of Section 1983 of the Civil Rights Act. *See Redondo-Borges v. United States Dep't of Hous. & Urban Dev.*, 421 F.3d 1, 7 (1st Cir. 2005). Likewise, it would also be unthinkable to deny Puerto Rico the right to restructure the debt of its public corporations while the other "states" are permitted to do so.

III. THE RECOVERY ACT IS NOT PREEMPTED BY CHAPTER 9 OF THE FEDERAL BANKRUPTY CODE

A. The Preemption Analysis of the Opinion Below is Erroneous and Usurps the Right of the Commonwealth of Puerto Rico to Exercise its Police Power to Protect its Citizens

While it is undisputed that Puerto Rico is not a State of the Union, it is by now settled that its laws enjoy the same standing in the federal system as those of any state. In *Calero-Toledo v. Pearson Yacht Leasing Co.*, 416 U.S. 663 (1974), this Court held that "Puerto Rico is to be deemed 'sovereign over matters not ruled by the Constitution.'" 416 U.S. at 673. *See also Examining Board of Engineers, Architects and Surveyors v. Otero*, 426 U.S. 572, 594 (1976) (Congress accorded Puerto Rico "the degree of autonomy and independence normally associated with States of the Union.").

As a result, it is unquestionable that Puerto Rico may exercise traditional state police powers on behalf of its citizens, and, when it exercises such powers, its legislation is subject to the same preemption analysis conducted regarding the laws of any state. Notwithstanding its "unique position" within the federal system *Puerto Rico Dept. of Consumer Affairs v. Isla Petroleum Corp.*, 485 U.S. 495, 499 (1988), the "... test for federal pre-emption of the law of Puerto Rico [ ] is the same as the test under the Supremacy Clause, U.S. Const., Art. VI, cl. 2." *Id.* at 499, (citing David J. Helfeld, *How Much of the United States Constitution and Statutes Are Applicable to the Commonwealth of Puerto Rico?* 110 F.R.D. 452, 469 (1985)).

Consequently, Puerto Rico is entitled to the same basic initial assumption that courts are required to make under federal law: absent that clear and manifest intent of Congress, a court must assume that Congress has not intended to displace state law.

In analyzing preemption cases, the court must start "with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." *International Paper Co. v. Ouellette*, 479 U.S. 481, 491 n.11 (1987). The clearest evidence of such intent to preempt is, of course, is an express provision in the statute preempting state law. *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977).

But that is not the only way in which a state law may be preempted. Preemption may also arise where Congress has occupied the field, *Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Commission*, 461 U.S. 190, 204 (1983), or when state law effectively conflicts with federal law. *Hillsborough County v. Automated Medical Laboratories, Inc.*, 471 U.S. 707, 713 (1985).

The conflict may exist because there is a "physical impossibility" to comply with both state and federal law, *Florida Lime and Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963), or where the state action is found to be "an obstacle to the accomplishment and execution of the full purposes and objectives of Congress". *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941).

In this case, there is no question that Congress has not occupied the field regarding Puerto Rico's ability to restructure the debts of its municipalities and public corporations because Congress expressly decided in 1984 to exclude Puerto Rico from Chapter 9 of the

Bankruptcy Code. Moreover, as it pertains to the restructuring of the debt of municipalities and public corporations in Puerto Rico, Congress has in effect withdrawn from the field. Consequently, and, a *fortiori*, a "physical conflict" between the Recovery Act and Chapter 9 of the Bankruptcy Code is not possible because there is no federal legislation on this particular matter that is applicable to Puerto Rico.

B. The Opinion Below Concedes that the Legislative History of the 1984 Amendments to the Bankruptcy Code is Silent as to the Reasons for the Exclusion of Puerto Rico from Chapter 9

Congress' silence does not provide the "clear and manifest" expression of congressional intent that is necessary to overcome the presumption against preemption. *California Federal Savings and Loan Association v. Guerra*, 479 U.S. 272, 288 (1987).

The guiding principle in the application of the Supremacy Clause must be the "respect for the separate spheres of governmental authority preserved in our federalist system." *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 19 (1987) (quoting *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 522 (1981)).

A court can ascertain Congressional intent to preempt state law by looking at various kinds of evidence of such intent. The strongest evidence of this intent is, of course, when Congress enacts a statute containing specific language that explicitly preempts state law. *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977). On the other hand, Congress may also show its intent to preempt state regulation by establishing a comprehensive federal regulatory scheme that at least ostensibly shows a congressional intent to occupy the field

of regulation in its entirety. See, e.g., *Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Commission*, 461 U.S. 190, 204 (1983); *Fidelity Federal Savings and Loan Association v. de la Cuesta*, 458 U.S. 141, 153 (1982).

But regardless of the approach taken by the court in determining the existence of preemption, "[t]he critical question . . . is *always* whether Congress intended that federal regulation supersede state law." *Louisiana Public Service Commission v. FCC*, 476 U.S. 355, 369 (1986) (emphasis added). And, this Court has repeatedly admonished that "courts should not lightly infer preemption." *International Paper Co. v. Ouellette*, 479 U.S. at 491, and have to start "with the basic assumption that Congress did not intend to displace state law." *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981).

In this case, there is simply no evidence of Congressional intent to encroach upon the traditional exercise of police powers by Puerto Rico.

C. The Opinion Below Failed to Consider the Most On-Point Precedent on the Correct Application of Preemption Analysis

The most on-point precedent for the determination of the correct preemption analysis applicable to this case is *Puerto Rico Dept. of Consumer Affairs v. Isla Petroleum Corp.*, 485 U.S. 495 (1988).

In this case, writing for a unanimous court, Justice Scalia delivered a clear and concise framework to conduct preemption analysis in cases involving Puerto Rico. Much like the instant case, in *Isla Petroleum*, *supra*, the District Court concluded that Congress had preempted Puerto Rico from regulating profit margins

for gasoline, notwithstanding the fact that Congress had decided to withdraw from the field.

Similarly, in this case, Congress decided to withdraw from the field of regulation of municipal bankruptcy for Puerto Rico in 1984. As a result, and just as in the *Isla Petroleum* case, the opinion below determined the existence of preemption on the basis of ". . . pre-empting legislation [that] was no more." *Id.* at 247. The application of the *ratio decidendi* of the *Isla Petroleum* case to the instant case should lead to the same result.

CONCLUSION

If Congress wants to prevent Puerto Rico from enacting legislation for the restructuring of the debt of its public corporations, it may do so under the Bankruptcy Clause. But courts, of course, cannot preempt anything. Only Congress can do that, subject to the limitations of the Tenth Amendment.

As a result, the enactment of the Recovery Act does not constitute an usurpation of the Congressional powers, but rather the exercise of traditional police power on the part of the Commonwealth of Puerto Rico in order to protect its citizens from the catastrophic consequences that will result from leaving its public corporations at the mercy of their creditors.

In the absence of any evidence of Congressional intent to preempt, Puerto Rico should be allowed to proceed with the implementation of the Recovery Act.

For the foregoing reasons, the *amici curiae* respectfully request that this Honorable Court reverse the decision of the United States Court of Appeals for the First Circuit.

Respectfully submitted.

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